Department of Water Resources
Electric Power Fund
Financial Statements

December 31, 2005

Department of Water Resources Electric Power Fund
Index

USING THIS REPORT

This discussion and analysis is designed to assist the reader in focusing on significant financial issues and activities and to identify any significant changes in financial position of the Department of Water Resources Electric Power Fund (Fund), which is administered by the California Department of Water Resources (DWR). Readers are encouraged to consider the information presented in conjunction with the financial statements as a whole, which follows *Management's Discussion and Analysis*. This discussion and analysis and the financial statements do not relate to DWR's other governmental and proprietary funds.

The basic financial statements include three required statements, which provide different views of the Fund. They are: the statement of net assets, the statement of revenues, expenses and changes in net assets and the statement of cash flows. These statements provide current and long-term information about the Fund and its activities. These financial statements report information using accounting methods similar (although not identical) to those used by private sector companies. The statement of net assets includes all assets and liabilities as of a specified date. The statement of revenues, expenses and changes in net assets presents all of the revenues and expenses for a specified time period. The final required statement is the statement of cash flows. This statement reports cash receipts, disbursements and the net change in cash resulting from three principal types of activities; operating activities, financing activities and investing activities. In order for the basic financial statements to be complete, they must be accompanied by a complete set of footnotes. The notes to the financial statements provide disclosures which are required to conform with generally accepted accounting principles. The Fund is required to follow accounting standards promulgated by the Governmental Accounting Standards Board.

This report should be read in conjunction with the Fund's June 30, 2005 audited financial statements.

BACKGROUND

The Fund was established in January 2001 through legislation to assist mitigation of the effects of a statewide energy supply emergency. DWR has the authority to secure and retain title to power for resale to end use customers of the State's investor owned utilities (IOUs) under power supply contracts entered into prior to January 1, 2003. On that date, DWR transitioned complete responsibility for the purchase of short-term power to the IOUs. DWR also transferred the scheduling, dispatch, and certain other administrative functions for the long-term contracts to the IOUs. However, DWR retains the legal and financial responsibility for the long-term contracts until such time as there is complete assignment of the contracts and release of DWR. DWR is entitled to recover its revenue requirements for authorized activities, including but not limited to debt service, the costs of power purchases, administrative costs and reserves.

STATEMENT OF NET ASSETS

The Fund's assets and liabilities as of December 31, 2005 and June 30, 2005 are summarized as follows (in millions):

	December		June	
Long-term restricted cash and investments	$	1,465	$	1,482
Recoverable costs, net of current portion		7,552		7,356
Restricted cash and investments:				
Operating and priority contract accounts		866		1,387
Bond charge collection and bond charge payment accounts		746		570
Other investments		173		80
Recoverable costs, current portion		620		573
Interest receivable		29		26
Total assets	$	11,451	$	11,474
Net assets	$	-	$	-
Long-term debt, including current portion		10,913		10,982
Accounts payable		470		424
Accrued interest payable		68		68
Total capitalization and liabilities	$	11,451	$	11,474

Long-Term Restricted Cash and Investments

The $555 million balance in the Operating Reserve Account at both December 31, 2005 and June 30, 2005 is determined in accordance with the bond indenture and represents twelve percent of projected annual operating expenses of the Fund for calendar year 2005. There was a decrease of $17 million to $910 million in the Debt Service Reserve Account during the six month period. The lower debt service reserve requirement results from reduced future annual debt service as a result of issuing refunding bonds as described in the Long-Term Debt section below.

Recoverable Costs, Net of Current Portion

Long-term recoverable costs consist of costs that are recoverable through future billings. The $196 million increase during the six month period ended December 31, 2005 is net of 1) operating expenses which exceed operating revenues by $457 million, and 2) bond charges plus interest income exceeding interest expense by $261 million.

Restricted Cash and Investments

The $866 million balance in the Operating and Priority Contract Accounts at December 31, 2005 is $76 million higher than forecast in DWR's 2005 Revenue Requirement determination, principally due to receipt of non-forecasted energy settlement monies earlier in the calendar year. The Operating and

Priority Contract Accounts had a net decrease of $521 million in the six months ended December 31, 2005 which is $176 million greater than forecast in the 2005 Revenue Requirement. In addition to the planned decrease in account balances, the additional decrease in cash is the result of higher than projected natural gas prices used to generate energy, partially offset by the collection of $96 million in energy settlements that were not forecast in the 2005 Revenue Requirement.

The Bond Charge Collection and Bond Charge Payment Accounts increased by $176 million during the six months ended December 31, 2005. The increase in the balances was expected in anticipation of the $409 million principal payment due in May 2006.

From the dates of issuance of the revenue bonds through December 31, 2005, the balances in each of the restricted cash and investments accounts met or exceeded balances required by the Bond Indenture.

Other Investments

Other investments consists of a brokerage account with a national brokerage firm in order to hedge natural gas costs for fuel used in the production of power under the terms of certain power purchase contracts.

Other investments increased by $93 million in the six months ended December 31, 2005 due primarily to realized gains. At December 31, 2005, the account consists of money market obligations, U.S. Treasury bills, and government bonds valued at $31 million and financial futures and options valued at $142 million. At December 31, 2005, DWR has open positions with an unrealized marked-to-market value increase of $10.3 million reflected in the account balance.

Recoverable Costs, Current Portion

The current portion of recoverable costs principally reflects billings to IOU customers that have not yet been collected. The current portion of recoverable costs at December 31, 2005, is higher than at June 30, 2005, because of the recognition of $83 million in energy settlements in December 2005 that were remitted to the Fund subsequent to December 31, 2005.

Long-Term Debt

In December 2005, DWR issued an aggregate $2.594 billion in variable rate refunding revenue bonds to advance refund $2.352 billion of outstanding 2002 Series A fixed rate bonds.

The proceeds of the refunding bonds, along with funds released from the Bond Charge Payment Account ($42 million) and Debt Service Reserve Account ($17 million), were used to purchase securities that were deposited in an irrevocable trust with an escrow agent to provide for future debt service payments on the advance refunded bonds and pay for underwriting fees and other issuance costs. As a result, the advance refunded bonds are considered to be defeased and the related liabilities have been removed from the financial statements.

In anticipation of the refunding, DWR entered into interest-rate swap agreements based on the London Inter-Bank Offered Rate (LIBOR) with a notional amount of $2.594 billion to pay fixed rates of interest and receive floating rate payments. The result is that the debt service on the refunding bonds is effectively fixed for the life of the bonds.

The refunding resulted in an accounting loss of approximately $218 million which has been deferred over the life of the refunded debt. However, the Fund effectively reduced its aggregate debt service payments by approximately $278 million through 2022 and achieved an economic gain (difference between the present values of the old and new debt service payments) estimated at the date of bond issuance to be $145 million. The actual economic gain will be dependent on basis risk associated with the interest rate swaps described in the preceding paragraph.

Accounts Payable

Accounts payable at December 31, 2005 are $46 million higher than at June 30, 2005 and reflect one month's accrual for power and gas purchases. The principal reason for the increase is higher gas prices.

Accrued Interest Payable

Accrued interest payable at both dates is substantially the same as they are for the same length of time in relation to the semi-annual payments for the fixed rate bonds and interest rate swaps.

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

The Fund's activities for the three months and six months ended December 31, 2005 and 2004 are summarized as follows (in millions):

	Three months ended December 31		Six months ended December 31	
	2005	**2004**	**2005**	**2004**
Revenues:				
Power charges	$ 923	$ 1,235	$ 1,793	$ 2,500
Surplus sales	102	95	241	160
Bond charges	208	209	424	452
Interest income	32	29	62	54
Total revenues	1,265	1,568	2,520	3,166
Expenses:				
Power purchases	1,513	1,376	2,653	2,802
Energy settlements	(179)	(96)	(179)	(96)
Interest expense	119	114	225	224
Other expenses	6	10	17	27
Recovery (deferral) of recoverable costs	(194)	164	(196)	209
Total expenses	1,265	1,568	2,520	3,166
Net income	-	-	-	-
Net assets, beginning of the period	-	-	-	-
Net assets, end of period	$ -	$ -	$ -	$ -

Power Charges

Revenues from power charges decreased by $707 million in the six months ended December 31, 2005 compared to the same period in 2004. The volume of power sold in the six month period ended December 31, 2005 is 11% less than sold in the same period in 2004, primarily because of the expiration of a major contract at December 31, 2004. Additionally, 2005 remittance rates, which are based on DWR's 2005 Revenue Requirement, are lower than the 2004 remittance rates. DWR was able to reduce remittance rates in calendar year 2005 to purposefully reduce the cash balance in the Operating Account and yet maintain balances in the Operating, Priority Contract, and Operating Accounts in excess of bond indenture requirements.

Surplus Sales

Revenues from surplus sales of energy increased by $81 million in the six months ended December 31, 2005 compared to the same period in 2004. Although the quantities of surplus energy sold are comparable during the two periods, the dollar value of sales of excess natural gas in 2005 reflects overall rising natural gas prices.

Bond Charges

Bond charges earned through December 31, 2005, were $28 million less than the same period in 2004. The reduction was the result of a lower bond charge rate in 2005 compared to the rate in place for the same period in 2004. The bond charges received have been adequate to meet all debt service requirements and maintain balances in the Bond Charge Collection, Bond Charge Payment, and Debt Service Reserve Accounts that are in excess of the bond indenture requirements.

Interest Income

There was an $8 million increase in interest income in the six months ended December 31, 2005 as compared to the same period in 2004 even though cash balances have decreased. The increase in interest income is attributable higher rates received on investments in the State of California Pooled Money Investment Account in the current period as compared to the same six month period in 2004.

Power Purchases

While the volume of power purchases in the six months ended December 31, 2005 is approximately 10% lower than in the same period in 2004, primarily reflecting the expiration of a contract at December 31, 2004, power costs are only 5% lower ($149 million) in the six month period ended December 31, 2005 than in the same period in 2004. This lower reduction in cost than in volume purchased reflects the higher gas prices for the generation of energy in the six months ended December 31, 2005 than in the same period in 2004, offset by a $93 million increase in value of the financial hedging portfolio during the six months ended December 31, 2005.

While power costs are lower for the six month period ended December 31, 2005 than in the same period in 2004, power costs are $137 million (10%) higher for the three month period ended December 31, 2005 than in the same period in 2004. In addition to increased gas prices over the three month period ended December 31, 2005, DWR also recognized a decrease in value of its financial hedging portfolio of $152 million due to decreasing forward prices. The decrease in the financial hedging portfolio in the three months ended December 31, 2005 offset the $245 million gain in the gas hedging portfolio in the three months ended September 30, 2005.

Energy Settlements

Energy settlements received, including those related to complex regulatory proceedings before the Federal Energy Regulatory Commission (FERC) arising from events in California energy markets in 2001, are recorded as a decrease in operating expenses.

Three energy settlements totaling $179 million were recognized in the three and six month periods ended December 31, 2005. First, as part of the energy settlement with Mirant Corporation in 2005, DWR received unsecured claims totaling $90 million plus accrued interest in the Mirant Corporation bankruptcy case. In December 2005, DWR sold its claims and received $96 million. Second, the energy settlement with Enron Corp. became effective and DWR recognized a $17 million energy settlement. This amount was included as a current recoverable cost at December 31, 2005 and the funds were subsequently received in January 2006. Other amounts owed from the Enron Corp. settlement are subject to bankruptcy court distributions and will be recognized as an energy settlement at such time as there is a distribution of monies. Finally, an energy settlement of $66 million with Reliant Energy became effective in December 2005 and is recorded as a current recoverable cost at December 31, 2005.

Interest Expense

Interest expense incurred during the six month period ended December 31, 2005 is substantially the same as in the same period in 2004.

Other Expenses

Administration expenses decreased $10 million in the six months ended December 31, 2005 compared to the same period in 2004 due to a reduction in statewide pro-rata cost allocation to the Fund and decreased costs incurred for contract renegotiation and litigation activities.

Recovery (Deferral) of Recoverable Costs

The individual components of the recovery (deferral) of recoverable costs for the three and six months ended December 31, 2005 and 2004 are summarized as follows (in millions):

	Three months ended December 31		Six months ended December 31	
	2005	**2004**	**2005**	**2004**
Operations	$ (315)	$ 40	$ (457)	$ (73)
Debt Service and related costs	121	124	261	282
	$ (194)	$ 164	$ (196)	$ 209

<u>Operations</u>
The $457 million deferral in the six months ended December 31, 2005 recognizes both the increases in natural gas costs, and DWR's ability to reduce power charges in calendar 2005 through the revenue requirement process, and still remain in compliance with Bond Indenture requirements.

Debt Service and Related Costs

The recovery of debt service and related costs are comparable between the six month periods ended December 31, 2005 and 2004, and are comprised solely of the difference between bond charges plus interest income less interest expense.

FUTURE OPERATIONS

In August 2005, the Governor introduced legislation that would establish a Department of Energy through the consolidation of the functions of several departments, commissions and offices that currently implement state energy programs. If the legislation were to be enacted, all of the powers, duties, responsibilities, rights, obligations, liabilities and jurisdiction of DWR under Division 27 of the California Water Code would be assumed by the Department of Energy.

DWR or its successor will administer the Fund at least until such time as the revenue bonds are completely retired. Revenue requirements for the repayment of the bonds will be determined at least annually and submitted to the California Public Utilities Commission (CPUC) for implementation. Under the terms of the rate agreement between the CPUC and DWR, the CPUC is required to set rates for the customers of the IOUs and "direct access" Electric Service Providers such that the Fund will always have monies to pay the principal of and interest on the bonds and all other bond related costs when due.

DWR has the authority to administer all power supply contracts entered into before December 31, 2002, for the life of the contracts. Over 95% of the volume of power under contract expires by December 31, 2011 and the last of the contracts is projected to expire in 2017. Revenue requirements for the payment of energy purchased under the contracts will be determined at least annually and submitted to the CPUC. Under the terms of the rate agreement between the CPUC and DWR, the CPUC is required to implement power charges such that the Fund will receive necessary monies to meet its revenue requirements.

The financial responsibility for the contracts may be transferred to the IOUs as part of a complete assignment of the contracts and release of DWR or its successor. However, there are a number of issues to be addressed, including IOU acceptance of the assignment and counterparty approval, before the contracts can be assigned.

Department of Water Resources Electric Power Fund
Statements of Net Assets
December 31, 2005 and June 30, 2005 (in millions)

	December 31, 2005	June 30, 2005
Assets		
Long-term assets:		
Restricted cash and investments:		
Operating Reserve Account	$ 555	$ 555
Debt Service Reserve Account	910	927
Recoverable costs, net of current portion	7,552	7,356
Total long-term assets	9,017	8,838
Current assets:		
Restricted cash and investments:		
Operating and Priority Contract Accounts	866	1,387
Bond Charge Collection and Bond Charge Payment Accounts	746	570
Other investments	173	80
Recoverable costs, current portion	620	573
Interest receivable	29	26
Total current assets	2,434	2,636
Total assets	$ 11,451	$ 11,474
Capitalization and Liabilities		
Capitalization:		
Net assets	$ -	$ -
Long-term debt:		
Revenue bonds	10,453	10,529
Total capitalization	10,453	10,529
Current liabilities:		
Current portion of long-term debt	460	453
Accounts payable	470	424
Accrued interest payable	68	68
Total current liabilities	998	945
Commitments and Contingencies (Note 5)		
Total capitalization and liabilities	$ 11,451	$ 11,474

The accompanying notes are an integral part of these financial statements

Department of Water Resources Electric Power Fund
Statements of Revenues, Expenses and Changes in Net Assets
For the three and six months ended December 31, 2005 and 2004 (in millions)

	Three months ended December 31		Six months ended December 31	
	2005	**2004**	**2005**	**2004**
Operating revenues:				
Power charges	$ 923	$ 1,235	$ 1,793	$ 2,500
Surplus sales	102	95	241	160
Total operating revenues	1,025	1,330	2,034	2,660
Operating expenses:				
Power purchases	1,513	1,376	2,653	2,802
Energy settlements	(179)	(96)	(179)	(96)
Administrative expenses	6	10	17	27
Recovery (deferral) of recoverable operating costs	(315)	40	(457)	(73)
Total operating expenses	1,025	1,330	2,034	2,660
Income from operations	-	-	-	-
Bond charges	208	209	424	452
Interest income	32	29	62	54
Interest expense	(119)	(114)	(225)	(224)
Recovery of recoverable debt service and related costs	(121)	(124)	(261)	(282)
Net income	-	-	-	-
Net assets, beginning of the period	-	-	-	-
Net assets, end of the period	$ -	$ -	$ -	$ -

The accompanying notes are an integral part of these financial statements

Department of Water Resources Electric Power Fund
Statements of Cash Flows
For the six months ended December 31, 2005 and 2004 (in millions)

	2005	2004
Cash flows from operating income:		
Receipts:		
Power charges	$ 1,822	$ 2,440
Surplus sales	248	201
Energy settlements	96	110
Payments for power purchases and other costs	(2,717)	(2,826)
Net cash used in operating activities	(551)	(75)
Cash flows from non-capital financing activities:		
Receipts from customers for bond charges	424	452
Interest payments	(235)	(245)
Proceeds from issuance of revenue bonds	2,594	-
Cost of issuance net of underwriters discount	(25)	-
Defeasance of revenue bonds	(2,628)	-
Net cash provided by non-capital financing activities	130	207
Cash flows from investing activities:		
Investments purchased	-	(50)
Interest received on investments	59	49
Net cash provided by (used in) by investing activities	59	(1)
Net (decrease) increase in restricted cash and investments	(362)	131
Restricted cash and investments, beginning of the period	3,439	3,381
Restricted cash and investments, end of the period	$ 3,077	$ 3,512
Reconciliation of operating income to net cash used in operating activities:		
Income from operations	$ -	$ -
Changes in net assets and liabilities to reconcile operating income to net cash used in operations:		
Recoverable costs	(597)	(61)
Accounts payable	46	(14)
Total adjustments	(551)	(75)
Net cash used in operating activities	$ (551)	$ (75)

The accompanying notes are an integral part of these financial statements.

December 31, 2005 (in millions)

1. Reporting Entity

Background
In January 2001, the Governor of California issued an emergency proclamation directing the Department of Water Resources (DWR) to enter into contracts and arrangements for the purchase and sale of electric power to assist in mitigating the effect of a statewide energy supply emergency.

The Department of Water Resources Electric Power Fund (a component unit of the State of California) (Fund), administered by the Department of Water Resources (DWR), was established in January 2001 through legislation adding Division 27 to the California Water Code.

DWR began selling electricity to approximately ten million IOU retail customers in California in January 2001. DWR purchases power from wholesale suppliers under long-term contracts and, through December 31, 2002, in short-term and spot market transactions. DWR power is delivered to the customers through the transmission and distribution systems of the IOUs and payments from the customers are collected for DWR by the IOUs pursuant to servicing arrangements approved and/or ordered by the CPUC.

Basis of Presentation
The Fund is accounted for as an enterprise fund and is financed and operated in a manner similar to that of a private business enterprise. The Fund uses the economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. As allowed by governmental accounting standards, the Fund has elected not to apply statements and related interpretations issued by the Financial Accounting Standards Board after November 30, 1989. The Fund is accounted for with a set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenses.

The financial statements of the Fund are intended to present the financial position, and the changes in financial position and cash flows, where applicable, of only that portion of the business-type activities and major funds of the State of California that is attributable to the transactions of the Fund. They do not purport to, and do not, present fairly the financial position of the State of California in conformity with accounting principles generally accepted in the United States of America.

2. Restricted Cash and Investments

As of December 31, 2005, $47 million of the Fund’s cash deposits was exposed to custodial credit risk as follows:

Institution	Amount	Custodial Credit Risk
Prime Value Obligations Fund Institutional Shares	$ 30	Insured
U.S. Bank	17	Uninsured and uncollateralized
	$ 47	

December 31, 2005 (in millions)

As of December 31, 2005, the Fund had the following investments:

Investment	Maturity	Fair Value
State of California Pooled Money Investment Account - State Money Investment Fund	5.5 months average	$ 2,460
Guaranteed investment contracts	May 1, 2022	500
Forward purchase agreement	May 1, 2006	100
Natural gas futures and options	3 months average	127
Other	5 year average	16
		$ 3,203

The Fund's investments in the guaranteed investment contracts (GIC) and forward purchase agreement (FPA) are rated as follows by Standard & Poor's (S&P) and Moody's, respectively, at December 31, 2005:

Investment	Amount	S&P	Moody's
GIC Providers			
FSA	$ 100	AAA	Aaa
XL Capital	150	AAA	Aaa
Royal Bank of Canada	100	AA-	Aa2
Sun America	150	AA+	Aa1
	$ 500		
FPA Provider			
Merrill Lynch: FHLMC Discounted Notes	$ 100	AAA	Aaa

3. Long-Term Debt

The following activity occurred in the long-term debt accounts during the six months ended December 31, 2005:

	Revenue Bonds	Unamortized Premium	Deferred Loss on Defeasance	Total Revenue Bonds
Balance, June 30, 2005	$ 10,696	$ 286	$ -	$ 10,982
Refunding				
Issuance of debt	2,594			2,594
Defeasance of debt	(2,353)	(72)	(218)	(2,643)
Amortization		(21)	1	(20)
Less current portion	(436)	(38)	14	(460)
Balance, December 31, 2005	$ 10,501	$ 155	$ (203)	$ 10,453

December 31, 2005 (in millions)

In December 2005, the Fund issued an aggregate $2,594 in Power Supply Revenue Bonds. The bonds issued were variable rate bonds and were comprised of the $759 Series F-Daily Rate Reset and $1,835 Series G-Weekly Rate Reset bonds. These bonds were used to refund $2,352 of outstanding fixed rate bonds, and to pay cost of issuance and certain costs of credit and liquidity enhancement.

The proceeds of the advance refunding bonds (after payment of underwriting refunding fees, other issuance costs) along with funds released from the Bond Charge Payment Account and Debt Service Reserve Account, were used to purchase securities that were deposited in an irrevocable trust with an escrow agent to provide for future debt service payments on the advance refunded bonds. As a result the advance refunded bonds are considered to be defeased and the related liabilities have been removed from the financial statements.

The advance refunding resulted in an accounting loss of approximately $218, which has been deferred over the life of the refunded debt. However, the Fund effectively reduced its aggregate debt service payments by approximately $278 through 2022 and obtained a net economic gain (difference between the present values of the old and new debt service payments) of $145. The actual economic gain will be dependent on basis risk associated with interest rate swaps that became effective and are further described in Note 4 to the financial statements.

The revenue bonds, all of which except series E are tax-exempt, consist of the following at December 31, 2005:

Series	Rates	Fiscal Year of Final maturity	Fiscal Year of First Call Date	Amounts Outstanding
A	3.0-6.0%	2022	2012	$ 3,843
B	Variable	2020	Callable	1,000
C	Variable	2022	Callable	2,750
D	Variable	2022	Callable	500
E	4.3%	2006	Not callable	250
F	Variable	2022	Callable	759
G	Variable	2018	Callable	1,835
				10,937
Plus unamortized bond premium				193
Less unamortized loss on bond redemption				(217)
Less current maturities				(460)
				$ 10,453

The interest rates for the variable debt for the six months ended December 31, 2005, ranged from 2.22% to 3.75%

December 31, 2005 (in millions)

Future payment requirements on the revenue bonds are as follows at December 31, 2005:

Fiscal Year	Principal	Interest [1]	Total
2006	$ 436	$ 224	$ 660
2007	448	431	878
2008	470	411	881
2009	493	389	882
2010	518	367	885
2011-2015	3,024	1,430	4,454
2016-2020	3,792	893	4,685
2021-2022	1,756	147	1,904
	$ 10,937	$ 4,292	$ 15,229

[1] Variable portion of interest cost calculated using the December 31, 2005 Bond Market Association Municipal Swap Index.

4. Interest Rate Swaps

The terms, fair values, and credit ratings of counterparties for the various swap agreements are summarized in the following table:

Outstanding Notional Amount	Fixed Rate Paid by Fund	Variable Rate [1] Received by Fund	Fair Value	Termination Date	Counterparty Credit Rating S&P	Counterparty Credit Rating Moody's	Counterparty Credit Rating Fitch
$ 94	2.914%	67% of LIBOR	$ 1	May 1, 2011	AAA	Aaa	AAA
234	3.024%	67% of LIBOR	3	May 1, 2012	AAA	Aaa	AAA
200	3.405%	BMA	1	May 1, 2013	A+	Aa3	A+
100	3.405%	BMA	-	May 1, 2013	A+	Aa3	AA-
30	3.405%	BMA	-	May 1, 2013	A+	Aa3	AA-
194	3.204%	67% of LIBOR	1	May 1, 2014	AA-	Aa1	AA-
355	3.184%	66.5% of LIBOR	-	May 1, 2015	AA-	Aa3	AA-
174	3.280%	67% of LIBOR	-	May 1, 2015	AAA	Aaa	AAA
202	3.342%	67% of LIBOR	(1)	May 1, 2016	AA	Aa2	AA
485	3.228%	66.5% of LIBOR	1	May 1, 2016	AA	Aa2	AA
202	3.389%	67% of LIBOR	(2)	May 1, 2017	A+	Aa3	AA-
480	3.282%	66.5% of LIBOR	1	May 1, 2017	AA-	A2	AA-
514	3.331%	66.5% of LIBOR	1	May 1, 2018	AA-	A3	AA-
306	3.256%	64% of LIBOR	1	May 1, 2020	AA-	A3	AA-
453	3.325%	64% of LIBOR	2	May 1, 2022	AA-	Aa2	AA
$ 4,024			$ 9				

[1] One month U.S. Dollar London Interbank Offered Rate or Bond Market Association Municipal Swap Index

The BMA and 67% of LIBOR swaps were effective in February 2003. All other swaps were effective December 1, 2005.

December 31, 2005 (in millions)

The notional amounts of the swaps match the principal amounts of the associated debt. The swap agreements contain scheduled reductions in notional amounts that follow scheduled amortization of the associated debt.

Fair Value: The reported fair values from the table above were derived from a combination of DWR valuations and those provided by the counterparties. Valuations use the par value, or marked-to-market, method.

Credit Risk: As of December 31, 2005, the Fund was not exposed to significant credit risk because the swaps had small positive and negative fair values.

Basis Risk: The Fund is exposed to basis risk on the swaps that have payments calculated on the basis of a percentage of LIBOR (a taxable rate index). As of December 31, 2005, the variable rate on DWR's hedged bonds ranged from 2.40% to 3.15%, while the variable rates received on the swaps were based on 64% to 67% of LIBOR and ranged from 2.810% to 2.941%.

Termination Risk: DWR's swap agreements do not contain any out-of-the-ordinary termination events that would expose it to significant termination risk.

Rollover Risk: Since the swap agreements have termination dates and notional amounts that are tied to equivalent maturity dates and principal amounts of amortizing debt, there is no rollover risk associated with the swap agreements, other than in the event of a termination.

Swap Payments and Associated Debt: As rates vary, variable-rate bond interest payments and net swap interest payments will vary. As of December 31, 2005, debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same, for their term were as follows:

	Variable Rate Bonds		Interest Rate	
Fiscal Year	**Principal**	**Interest**	**Swaps, Net**	**Total**
2006	$ -	$ 71	$ 6	$ 77
2007	-	141	13	154
2008	-	141	13	154
2009	-	141	13	154
2010	-	141	13	154
2011-2015	1,381	638	63	2,082
2016-2020	2,190	259	32	2,481
2021-2022	453	32	5	490
	$ 4,024	$ 1,564	$ 158	$ 5,746

5. Commitments and Contingencies

Litigation

DWR is involved in lawsuits and regulatory proceedings that could impact power costs and future revenue requirements.

In July, 2001, the Federal Energy Regulatory Commission (FERC) initiated a proceeding to calculate refunds for inflated prices in the California Independent System Operator (CAISO) and California Power Exchange Corporation markets during 2000 and 2001. DWR purchased $2.9 billion in energy to meet the CAISO's emergency needs during 2001. DWR is treated in the FERC refund proceeding as a seller of that energy to CAISO, and in May 2004, FERC issued an order requiring DWR to pay refunds on the $2.9 billion in "sales" to the CAISO. The refund amount totals approximately $2.2 billion on a gross basis, of which DWR could actually owe up to approximately $150 million on a net basis, because DWR would be the primary recipient of the refunds FERC required DWR to pay. However, FERC also later ruled that, like all sellers, to the extent DWR could demonstrate that payment of the refunds would result in DWR's costs exceeding its revenues, DWR could request FERC to reduce the refunds that would be owed. DWR sold all energy to the CAISO at its cost of acquisition. In September 2005, DWR made a cost recovery filing to request such a reduction in its refund obligation. Should the Fund be required to pay any refunds as a result of this FERC proceeding, the refunds would be recoverable from ratepayers through future revenue requirements.

There are a number of lawsuits and regulatory proceedings in which DWR is not a party but may be affected by the result. In one consolidated set of cases, the issue is whether and to what extent compensation is due from the State of California as a result of the State's commandeering of certain block forward contracts in early 2001. Certain market participants claim that they are entitled to damages in excess of $1 billion, their estimation of the fair value of the block forward contracts at the time of commandeering. DWR paid approximately $352 million for energy provided under the contracts, which expired in December 2001. Given the early state of the proceeding, it is not possible to predict or determine the outcome of this matter or to provide an estimate of any losses, if any, that may arise. However, management believes that the costs associated with this action will not have a material adverse effect on the Fund's financial position or liquidity. Should the Fund be determined to be the source of moneys to pay any damages resulting from this litigation, those damages would be recoverable from ratepayers through future DWR revenue requirements.

Management believes that the existing lawsuits and regulatory proceedings will be resolved in the fiscal year. Because of the early stage of the legal and regulatory proceedings, the ultimate outcome of these matters cannot be presently determined.

Commitments

DWR has power purchase contracts that have remaining lives of up to ten years. Payments made under these contracts approximated $2.7 billion and $2.8 million for the six months ended December 31, 2005 and December 31, 2004, respectively.

December 31, 2005 (in millions)

The remaining amounts of fixed obligations under the contracts as of December 31, 2005, are as follows:

Fiscal Year	Fixed Obligation
2006	$ 1,179
2007	2,525
2008	2,379
2009	2,238
2010	1,805
Thereafter	1,638
	$ 11,763

In addition to the fixed costs there are variable costs under several of the contracts. Management projected as of December 31, 2005 that the amount of future fixed and variable obligations associated with long-term power purchase contracts would approximate $24 billion. The difference between the fixed costs and the expected total costs of the contracts are primarily due to the variable factors associated with dispatchable contracts and the cost of natural gas.

6. Energy Settlements

DWR and other parties have entered into settlement agreements with various energy suppliers which resolve potential and alleged causes of action against suppliers for their part in alleged manipulation of natural gas and electricity commodity and transportation markets during the 2000 - 2001 California energy crisis.

Three energy settlements totaling $179 were recognized in the three and six month periods ended December 31, 2005. First, as part of the energy settlement with Mirant Corporation in 2005, DWR received unsecured claims totaling $90 plus accrued interest in the Mirant Corporation bankruptcy case. In December 2005, DWR sold its claims and received $96 million. Second, the energy settlement with Enron Corp. became effective and DWR recognized a $17 energy settlement. This amount was included as a current recoverable cost at December 31, 2005 and the funds were subsequently received in January 2006. Other amounts owed from the Enron Corp. settlement are subject to bankruptcy court distributions and will be recognized as an energy settlement at such time as there is a distribution of monies. Finally, an energy settlement of $66 with Reliant Energy became effective in December 2005 and is recorded as a current recoverable cost at December 31, 2005.